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SIPDIS

DEPARTMENT FOR INL, WHA/CEN, and EB/ESC/TFS
JUSTICE FOR OIA, AFMLS
TREASURY FOR FINCEN
DEA FOR OILS AND OFFICE OF DIVERSION CONTROL

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SUBJECT: COSTA RICA INCSR REPORT 2005 - 2006 PART II, MONEY LAUNDERING AND FINANCIAL CRIMES

REF: SECSTATE 210351

Draft text of the 2005-2006 INCSR, Part II for Costa Rica follows.
Costa Rica
Costa Rica is not a major financial center, but it remains vulnerable to money laundering and other financial crimes, due in part to narcotics trafficking, particularly of South-American cocaine, in the region and the presence in Costa Rica of Internet gaming companies. Reforms to the Costa Rican counternarcotics law in 2002, which expand the scope of anti-money laundering regulations, also create a loophole by eliminating the government's licensing and supervision of casinos, jewelers, realtors, attorneys, and other non-bank financial institutions. No actions were taken to close this loophole in 2005. Gambling is legal in Costa Rica, and there is no requirement that the currency used in Internet gaming operations be transferred to Costa Rica. Currently, over 250 sports-book companies have registered to operate in Costa Rica. Many of these registered firms have the same owners and addresses.
In 2002, the Government of Costa Rica (GOCR) expanded the scope of Law 7786 via Law 8204. This expansion criminalizes the laundering of proceeds from all serious crimes. Serious crimes are defined as carrying a sentence of four years or more. Law 8204, which is a counter-narcotics law, also obligates financial institutions and other businesses (such as money exchangers) to identify their clients, report currency transactions over $10,000, report suspicious transactions, keep financial records for at least five years, and identify the beneficial owners of accounts and funds involved in transactions. While Law 8204, in theory, covers the movement of all capital, current regulations based on Law 8204, Chapter IV, Article 14, apply a restrictive interpretation that covers only those entities that are involved in the transfer of funds as a primary business purpose.
The formal banking industry in Costa Rica is tightly regulated. However, the offshore banking sector that offers banking, corporate, and trust formation services remains open and is an area of concern. Foreign-domiciled "offshore" banks can only conduct transactions under a service contract with a domestic bank, and they do not engage directly in financial operations in Costa Rica. Costa Rican authorities acknowledge that they are unable to adequately assess risk. The Office of the Superintendent of Financial Institutions (SUGEF) regulates Costa Rican financial institutions.
Currently, six offshore banks maintain correspondent operations in Costa Rica, three from the Bahamas and three from Panama. The GOCR has supervision agreements with its counterparts in Panama and the Bahamas, permitting the review of correspondent banking operations. Unfortunately, these counterpart regulatory authorities occasionally interpret the agreements in ways that limit review by Costa Rican officials. In September 2005, the GOCR's Attorney ("Procurador General") ruled that SUGEF has no authority to regulate offshore operations. The ruling was an attempt to clarify apparent contradictions between the 1995 Organic Law of the Costa Rican Central Bank and Law 8204. Draft legislation to correct the contradiction and reassert SUGEF's regulatory power is under review in the Legislative Assembly. However, important legal initiatives often languish in the Legislative Assembly for years.
All persons carrying cash are required to declare any amount over $10,000 to Costa Rican officials at ports of entry. During 2005, officials seized over $850,000, much of it in undeclared cash. In 2004, the GOCR seized $1.2 million.
Eighteen free trade zones operate within Costa Rica, primarily producing electronic components, integrated circuits, textiles, and medicines for re-export. The Zones are under the supervision of "PROCOMER" an export-promotion entity. Costa Rican authorities report no indications of trade-based money laundering schemes in the zones. PROCOMER strictly enforces control over the zones, but its measures are aimed primarily at preventing tax evasion.
Costa Rica's Financial Intelligence Unit (FIU) became operational in 1998 and was admitted into the Egmont Group in 1999. The unit is analytical, screening cases for referral to prosecutors. The FIU has access to the records

and databases of financial institutions and other government entities but must obtain a court order if the information collected is to be used as evidence in court. The unit has no regulatory responsibilities. Despite its committed and professional staff, the unit remains ill equipped and under-funded to handle its current caseload (over 120 cases for 2005) and to provide the information needed by investigators. Nevertheless, the unit developed evidence it considers formidable in four high-profile cases of money laundering during 2004. Three of those cases were successfully prosecuted in 2005. Three additional money-laundering cases began judicial proceedings in 2005 and the FIU assisted international investigators to develop evidence in four more cases.

Costa Rican authorities have received and circulated to all financial institutions the lists of individuals and entities designated by the U.S. or EU, or considered by the UN 1267 Sanction's Committee to be involved in the financing of terrorism. However, these authorities cannot block, seize, or freeze property without prior judicial approval. Thus, Costa Rica lacks the ability to expeditiously freeze assets connected to terrorism. No assets related to designated individuals or entities were identified in Costa Rica in ¶2005. An interagency effort is underway to reduce the time required to obtain such judicial approval.

The GOCR has ratified the major UN counterterrorism conventions. Additionally, a government task force drafted a comprehensive counterterrorism law with specific terrorist financing provisions in 2002. The draft law would expand existing conspiracy laws to include the financing of terrorism. It would also enhance existing narcotics laws by incorporating the prevention of terrorist financing into the mandate of the Costa Rican Drug Institute. In 2004, the Legislative Assembly considered a separate draft terrorism law. In July of 2005, the Assembly's Narcotics Committee approved a bill combining the two proposals, but no further progress has been made.

Costa Rica is a party to the 1988 UN Drug Convention, the UN International Convention for the Suppression of the Financing of Terrorism, and the UN Convention against Transnational Organized Crime. The GOCR has signed, but not yet ratified, the UN Convention against Corruption. The GOCR has also signed the OAS Inter-American Convention on Mutual Assistance in Criminal Matters, and is a member of the Caribbean Financial Action Task Force (CFATF) and the aforementioned Egmont Group.